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Inclusion v. Idaho Dept of Health and Welfare Appellant's Brief Dckt. 42245

IN THE SUPREME COURT OF THE STATE OF IDAHO

INCLUSION INC. an Idaho corporation, INCLUSION NORTH, INC., an Idaho corporation, and INCLUSION SOUTH, INC., an Idaho corporation, Plaintiffs-Appellants-Cross-Respondents, v. IDAHO DEPARTMENT OF HEALTH AND WELFARE and RICHARD ARMSTRONG, Defendants-Respondents-Cross-Appellants.	**Supreme Court No. 42245**

CROSS-APPELLANTS' OPENING BRIEF

Appeal from the District Court of the Fourth Judicial District
of the State of Idaho, in and for the County of Ada
Case No. CV OC 2012-16467

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Honorable Richard D. Greenwood, District Judge, presiding

LAWRENCE G. WASDEN
ATTORNEY GENERAL

STEVEN L. OLSEN, ISB #3586
Chief of Civil Litigation

CARL J. WITHROE, ISB #7051
Deputy Attorney General
954 W. Jefferson Street, 2nd Floor
P.O. Box 83720
Boise, ID 83720-0010
Telephone: (208) 334-2400
Facsimile: (208) 854-8073
Attorney for Defendants-Appellants

DENNIS M. CHARNEY
Charney and Associates, PLLC
1191 East Iron Eagle Drive
Eagle, ID 83616
Telephone: (208) 938-9500
Facsimile: (208) 938-9504
Attorney for Plaintiffs-Respondents

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STATEMENT OF THE CASE

I. Nature of the Case

This is yet another appeal about attorney fees. It presents the question whether a prevailing party entitled to a "reasonable" attorney fee under Idaho Code § 12-120(3) may recover no more than the amount that party spent on its attorneys, even where the district court determines the hourly rate and time expended were reasonable. The cross-respondents, a group of Medicaid providers, sued the cross-appellants, the Idaho Department of Health and Welfare and its Director, claiming the Department's reimbursement rates were too low. The providers raised breach-of-contract and other contract-related claims, and the district court granted the Department's motion for summary judgment on all counts. The Department sought attorney fees under Idaho Code § 12-120(3). It requested a rate of $125 an hour for an attorney with 12-plus years' experience—a bargain given the going rate in the market in 2014. The district court found the time spent and hourly rate reasonable, but declined to award fees at $125 an hour.

Instead, the court ruled that even where $125 an hour is a market-reasonable rate, a party may not recover attorney fees that exceed the actual cost of its lawyers:

> Except where the award of attorney fees is paid to the lawyer, fees awarded to a party should not exceed the amount the client actually paid for the lawyer. This is so whether the prevailing party is a government entity or private party. To do otherwise is an impermissible penalty and does not serve the purpose of simply making the receiving party whole.

Replacement R. p. 125.[1] This broad limitation finds no support in the text of Idaho Code § 12-

[1] A note about citations to the record: Throughout this brief, reference will be made to the Clerk's Record on Appeal and the Replacement Limited Clerk's Record on Appeal. The plaintiff

120, and is inconsistent with this Court's cases applying Idaho R. Civ. P. 54(e)(3). The district court's order on attorney fees and amended judgment should be reversed.

II. The Facts

A. Prologue: The Federal Case That Spawned This Case

To put this case in the proper context, we have to begin in federal court in 2009, when a group of Medicaid providers sued Idaho Medicaid officials in federal court seeking higher Medicaid reimbursement rates under a federal Medicaid reimbursement statute. They had no rights enforceable through 42 U.S.C. § 1983 or the Social Security Act (of which Medicaid is a part), but Ninth Circuit law at the time permitted private enforcement actions like the providers' through the Supremacy Clause of the U.S. Constitution. And, at the time, a Ninth Circuit case, *Orthopaedic Hospital v. Belshe*, 103 F.3d 1491 (9th Cir. 1997), required states to conduct cost studies before adjusting Medicaid reimbursement rates and required that rates bear a reasonable relationship to actual provider costs. The Department had conducted cost studies since 2006, and proposed to raise rates, but the Idaho Legislature did not appropriate funds for rate increases. *Inclusion, Inc. v. Armstrong*, 835 F. Supp. 2d 960 (D. Idaho 2011). The providers argued that the rates, therefore, were not based on cost study information and did not bear the necessary relationship to provider costs. The U.S. District Court agreed, and held that based on

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Medicaid providers filed a notice of appeal from the judgment on the merits. The Clerk's Record was prepared, lodged, and settled before the plaintiffs voluntarily dismissed their appeal. References to the Clerk's Record will appear as "R" followed by the page number. A limited record was prepared at the Department's request for its cross-appeal of the district court's order on attorney fees. That limited record was augmented at the Department's request and will be cited as "Replacement R" followed by the page number.

Orthopaedic Hospital, the rates were preempted by the Medicaid statute. *Id.* It issued an injunction requiring the Department to raise its reimbursement rates. The Ninth Circuit affirmed in April 2014. *Exceptional Child Center, Inc. v.* Armstrong, 567 Fed. Appx. 496 (9th Cir. Apr. 4, 2014).

B. This Case

Meanwhile, *this* case was filed in 2012. R. p. 7. Under the Eleventh Amendment, the plaintiffs in the federal case could not recover back payments in federal court. So some of those plaintiffs from the federal case filed this case in state court and asserted the Department breached its contract with the providers by reimbursing them at rates the federal district court ultimately said were too low. R. pp. 14-15. They sought back payment dating back to the breach-of-contract statute of limitations—five years—totaling nearly $11,000,000. R. pp. 15-16. The Department defeated the providers' motion for summary judgment, R. pp. 589-92, and near trial, the court allowed the providers to amend their complaint and re-set trial. R. pp. 594-606. The Department then filed a motion for summary judgment in February 2014. R. pp. 615-16.

A day after the Ninth Circuit affirmed the federal district court's judgment in the federal case, the district court in this case issued a decision granting summary judgment in the State's favor on all counts. R. pp. 951-61. The State filed a motion for attorney fees and a supporting memorandum and affidavit of counsel, seeking $74,925.00 for 599.4 hours of attorney work at

$125 an hour. Replacement R. pp. 9-37.[2] Once the district court judgment issued on the merits phase, the providers filed a notice of appeal, but that appeal was dismissed by the parties' stipulation in October 2015.

C. The Federal Case Goes to the U.S. Supreme Court

With the Department's motion for attorney fees pending in state court, the State filed a petition for *certiorari* in the federal case in July 2014. The U.S. Supreme Court granted the petition in October 2014 and the case was argued in January 2015. The Supreme Court held in March 2015 that the Supremacy Clause does not establish a private cause of action, and that the Medicaid providers may not maintain their suit against the State. *Armstrong v. Exceptional Child Ctr., Inc.*, 135 S. Ct. 1378 (2015). It reversed the Ninth Circuit's judgment. The federal district court's decision and injunction ordering the rates to be increased was vacated on remand in September 2015, and the plaintiffs' complaint was dismissed with prejudice for failure to state a claim.

D. The Motion for Attorney Fees in This Case

1. In response to the Department's fee petition, the providers argued it was unfair for the Department to recover fees at $125 an hour since the attorney's salary was well below that, and since the Attorney General's office only billed agencies $54 an hour.[3] The $54-

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[2] The Attorney General's policy is to seek to recover attorney fees at various rates depending on the years of experience for the particular lawyer. For the lawyer in this case, the policy rate was $125.

[3] The providers also argued that fees were unavailable under Idaho Code § 12-120(3) because this case did not concern a commercial transaction. But the providers' claims arose from the parties' agreement that the providers would provide Medicaid services in exchange for payment

an-hour rate came from a letter from a member of the Idaho House of Representatives to the State Office of Performance Evaluations submitted by the providers in their papers opposing the Department's fee request. That letter (which concerned litigation unrelated to this case) suggested the rate for deputy attorneys general is $54 an hour. Replacement R. pp. 59-60. Though no one is sure, the state representative was likely referring to the rate established by the state Division of Financial Management as part of its Statewide Cost Allocation Program, or SWCAP. SWCAP was developed by the Division of Financial Management as a cost-allocation mechanism required by the federal government for administering and cost-tracking of federal-state programs and grants. Replacement R. pp. 81-84. The criteria for eligible costs is outlined in a circular published by the federal Office of Management and Budget. Replacement R. p. 82. The Attorney General, by statute, charges for services rendered to State departments. Idaho Code § 67-1408. Every year, the Attorney General reports time billed to each agency to the Division of Financial Management. Replacement R. p. 83. The Division of Financial Management, in turn, calculates the cost per hour for the Attorney General's services using the SWCAP criteria, and submits a bill to the agency. Replacement R. p. 83. The agency then pays that amount into the Indirect Cost Recovery Fund, and then that money is then transmitted into the general fund. Replacement R. p. 83; *see also* Idaho Code § 67-1407.

2. At the first hearing on attorney fees in the state court case, the district judge asked the Department's lawyer just where the money for attorney fees went and how the

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by the Department. The district court accordingly found that this case involved a commercial transaction and the providers have not appealed that ruling.

Attorney General billed client agencies. The judge explained that if the fee award exceeded the actual cost of the lawyers, it would violate a rule of attorney professional conduct prohibiting fee-sharing with non-lawyers. Tr. (Dec. 3, 2014) pp. 34, L. 13-p. 39, L. 9. The court allowed the Department to file an affidavit explaining what the actual cost to the Department was for its use of a deputy attorney general. Tr. (Dec. 3, 2014) p. 40, L. 15. It did not allow briefs. Tr. (Dec. 3, 2014) p. 41, L. 2; Replacement R. p. 79. The Department filed an affidavit of an official at the state Division of Financial Management explaining SWCAP (Replacement R. pp. 81-84) and sought the court's leave to file briefing on the issue, since no party had raised it (Replacement R. p. 79). The court issued a short decision, reasoning that lawyers may not share fees with the client, and so to award attorney fees based on the prevailing market rate would violate the rules of professional conduct.[4] Replacement R. pp. 88-91. A judgment issued on February 10, 2015. Replacement R. p. 92.

The Department filed a timely motion to reconsider. Replacement R. pp. 94-95. In its decision the court retreated from what it perceived as a fee-sharing problem, and ruled instead that the Department could only recover the SWCAP rate because to recover more would produce

[4] The Rule of Professional Conduct at issue was 5.4, which prohibits lawyers from sharing attorney fees with non-lawyers. Under § 12-120(3), the party, not the lawyer, is entitled to the fee award. Rule 5.4 is aimed at protecting clients by preventing interference with the attorney-client relationship that may arise if the lawyer shares fees with non-lawyer, non-client third parties. If the lawyer may agree to share fees with non-client, non-lawyer third-parties, the outside interest in the litigation may compromise the lawyer's independent judgment and the lawyer's obligations to the client. But here, the fee is the property of the client, and an award to the client in excess of the amount it paid does not constitute fee-sharing that is prohibited by Rule 5.4. *See, e.g., Central States, Se. & Sw. Areas Pension Fund v. Central Cartage Co.*, 76 F.3d 114 (7th Cir. 1996).

a windfall to the Department and exact a penalty on the providers. The Department filed its Notice of Cross-Appeal on September 16, 2015. Replacement R. pp. 127-29.

ISSUES PRESENTED

1. Whether Idaho Code § 12-120(3), which entitles a prevailing party in certain cases to "a reasonable attorney's fee," and Idaho R. Civ. P. 54(e)(3), which lists several factors for a district court to consider in awarding attorney fees, limits that recovery to no more than the amount the party spent for its attorneys to litigate the case.

2. Whether, if the Department prevails in this appeal, it is entitled to recover attorney fees from the providers under Idaho Code § 12-120(3).

STANDARD OF REVIEW

A district court's award of attorney fees and costs is within the discretion of the trial court and subject to review for an abuse of discretion. *See Burns v. Baldwin*, 138 Idaho 480, 486, 65 P.3d 502, 508 (2003); *Smith v. Mitton*, 140 Idaho 893, 897, 104 P.3d 367, 371 (2004). Generally, under the abuse-of-discretion standard, the Court reviews the lower court's ruling to determine whether (1) the court perceived the matter as within its discretion; (2) acted within the outer boundaries of its discretion and consistently with the legal standards applicable to the specific choices available to it; and (3) reached its decision by an exercise of reason. *Read v. Harvey*, 147 Idaho 364, 369, 209 P.3d 661, 666 (2009).

This case involves prong two of that inquiry—whether the district court's ruling was consistent with the applicable legal standards in Idaho Code § 12-120 and Idaho R. Civ. P. 53(e)(3). The meaning of an attorney-fee statute is subject to free review, *Smith v. Washington*

County, 150 Idaho 388, 389, 247 P.3d 615, 616 (2010), as is the application of a rule of procedure, *Zenner v. Holcomb*, 147 Idaho 444, 450, 210 P.3d 552, 558 (2009).

ARGUMENT

I. The District Court Abused Its Discretion by Capping a Prevailing Party's Recovery of Attorney Fees to No More Than the Party Spent on its Lawyers

The district court found that 599.4 hours was a reasonable amount of time to spend on the case. And the court found that $125 an hour was a reasonable rate for an attorney with 12 years' experience in the Boise market. The providers did not contest the objective reasonableness of that rate either. They contended instead that in this case, the Department should only be entitled to recover the amount it cost the Department to litigate the case, because to award more was a "windfall" to the State and a penalty to them. The district court did not say whether the limitation it imposed on the recovery of attorney fees was rooted in Idaho Code § 12-120 or in Idaho R. Civ. P. 54(e) or a decision of this Court or the Court of Appeals. Rather, it based its decision on its perception of the relative equities of awarding the Department market-rate fees. To do this, the district court read into the statute and rule a limitation not found in either. The district court therefore applied the wrong legal standard and so abused its discretion. *See Kirham v. 4.60 Acres of Land in Vicinity of Inkom*, 100 Idaho 781, 785, 605 P.2d 959, 963 (1980).

A. The District Court's Ruling Conflicts With the Plain Language of Idaho Code § 12-120(3) and the Court's Cases Applying Idaho R. Civ. P. 54(e)(3)

1. This appeal presents a matter of statutory construction. Section 12-120(3) allows a "reasonable" attorney fee to the prevailing party and reasonableness is the "bottom line" in making that award. *Lettunich v. Lettunich*, 145 Idaho 746, 750, 185 P.3d 258, 262 (2008).

Idaho R. Civ. P. 53(e) directs the court's search for reasonableness, enumerating 12 factors for the court to consider. To demonstrate the reasonableness of its request for $74,925.00, the Department submitted a memorandum of costs and a supporting affidavit showing that $125 an hour was reasonable in the geographic market and for the experience of the attorney handling the case. Replacement R. pp. 11-37. The affidavit provided the district court with time records to show how much time was expended and how that time was spent. The Court found that both the rate and the time expended were reasonable. But, in spite of these uncontroversial findings, the district court ruled as a matter of law that "the best measure of reasonable attorney fees" was the cost of the lawyer's services to the client. Replacement R. p. 124. The court explained that a measure other than the amount the client actually paid the lawyer effected a "windfall profit" to the winner and a penalty to the loser. Replacement R. p. 124, 125. So even though the hours were reasonable, the hourly rate was not. It capped the rate at $51.48 an hour for a total of $30,857.11.[5]

2. This ruling, capping the recoverable hourly rate to the amount the client spent on its lawyer, effectively reads into § 12-120(3) a limitation that does not appear in the text of the statute. This Court has disapproved the practice of engrafting onto statutes requirements the Legislature did not write. *Parsons v. Mut. of Enumclaw Ins. Co.* 143 Idaho 743, 746, 152 P.3d 614, 617 (2007). *Parsons* illustrates why the district court's fee recovery cap is improper. The Court in *Parsons* rejected an insurance company's argument that the Court should revive a

[5] $51.48 was the SWCAP amount for fiscal year 2013. Replacement R. p. 83. The Fiscal Year 2014 SWCAP rate had not yet been developed when the SWCAP amount became an issue as to

judicially created (and later abandoned) requirement of an insurance code attorney fees statute, Idaho Code § 41-1839. That statute provides that an insurer who fails to pay its insured the "amount justly due" under the policy within 30 days after proof of loss is furnished must pay attorney fees in an action against the insurer. Idaho Code § 41-1839(1). In 1968, the Court held that there must be evidence that an insurer acted unreasonably or unjustly in order for a party to receive attorney fees. 143 Idaho at 746, 152 P.3d at 617. But, five years later, recognizing it had engrafted an unwarranted requirement to the statute, it dumped that rule. *Id.* Then, in 1997, the Court read § 41-1839 to allow fees only when the insured had "no option other than to file suit against his or her insurer in order to recover his or her loss." *Id.* But that requirement does not appear in the statute, and so in 2002, the Court reversed course, again retreating from a case where it had added a requirement not found in the text. *Id.* The Court explained that "[a]rguments for additional requirements not contained in the statutory language must be made to the legislature, not this Court." *Id.* at 747, 152 P.3d at 618; *see also Estate of Holland v. Metropolitan Prop. & Cas. Ins. Co.*, 153 Idaho 94, 279 P.3d 80 (2012) (rejecting district court requirement that knowledge of suit by insurance company was necessary to demonstrate insured was prevailing party under Idaho Code § 41-1839; nothing in the "wording of statute that would make knowledge of the lawsuit a relevant factor in determining entitlement to attorney fees").

In short, the district court in this case did the same thing that this Court has held against. Nothing in § 12-120(3) supports the district court's view that a "reasonable" attorney fee is limited to the client's obligation. Those are two things that are not necessarily the same. The

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the amount of fees the Department could recover. *Id.*

Court has never held that they are. In fact, the Court has recognized that "actual" attorney fees are not necessarily "reasonable" attorney fees. *See Zenner v. Holcomb*, 147 Idaho at 450-51, 210 P.3d at 558-59 (trial court attorney fee award of "actual" attorney fees, where contract between litigants allowed "actual" fees, was not error; to apply reasonableness criteria from Rule 53(e) would be inconsistent with contract calling for "actual" fees). There is good reason not to read into § 12-120 the limitation the district court did. Section 12-120(3) reflects the Legislature's choice to allocate on a reasonableness basis the obligation of attorney fees to the party that loses a case. The Legislature did not, by contrast, choose to limit attorney fees to those actually expended by the client. The choice to award reasonable attorney fees in that manner should be given effect. Surely the Legislature can write the words necessary to limit attorney fees in the manner the district court envisioned. Because it did not, this Court should follow its practice of rejecting judicially created additions to plain statutory language.

3. It is enough that the district court engrafted a limitation onto the statute that finds no support in the text of it. But the Court has already explained that a fee award is not necessarily tied to the agreement between client and lawyer, and may be more or less than what the client agreed to pay the lawyer. *See Ada County Hwy. Dist. v. Acarrequi*, 105 Idaho 873, 878, 673 P.2d 1067, 1072 (1983), *overruled in part on other grounds*, *Dep't of Transp. v. Grathol*, 158 Idaho 38, 343 P.3d 480 (2015) (in condemnation action, Rule 54(e) factors are appropriately considered; but "[w]e caution that the court should not automatically adopt any contingent fee or contractual arrangement, but rather the fee awarded may be more or less than that provided in the lawyer-client contract"). Five years after *Acarrequi*, the Court of Appeals

held that if a prevailing party has a contingency fee agreement, and the statute at issue allows for "reasonable" fees, the fee award need not necessarily conform to that agreement: "we have previously ruled that a court is *not* prohibited from allowing recovery to the prevailing party in excess of the amount which the party is contractually obligated to pay his attorney." *Nalen v. Jenkins*, 114 Idaho 973, 976, 114 P.2d 1081, 1084 (Ct. App. 1988), *citing Decker v. Homeguard Systems*, 105 Idaho 158, 666 P.2d 1169 (Ct. App. 1983).

A more recent case, *Griffith v. Clear Lakes Trout Co., Inc.*, 146 Idaho 613, 200 P.3d 1162 (2009), shows, too, that the fee award need not match the fee agreement. There, the prevailing party sought fees on an hourly basis for its first appeal, and sought an award based on the contingency agreement for the second one. *Id.* at 617, 200 P.3d at 1166. The losing side argued it was inequitable to allow the prevailing party to switch the basis of its fee request, but the Court disagreed. It acknowledged the "harsh result" of burdening the losing side with the other's attorney fees but stressed that the district judge's eye should be on the reasonableness of the amount, whatever the basis for it. *Id.* at 623, 200 P.2d at 1172.

The Court has held, too, that a party entitled to recover a reasonable attorney fee may recover even though it did not *actually* incur *any* attorney fees at all. In *Dunmire v. Dunlap*, 100 Idaho 697, 604 P.2d 711 (1979), the Court held that salaried staff lawyers with a legal aid organization who were appointed by the court in a Youth Rehabilitation Act case were entitled to recover from the county reasonable attorney fees under a statute allowing for "reasonable compensation," just the same as outside, private counsel could. *Id.* at 699-700, 804 P.2d at 713-14. Citing *Dunmire v. Dunlap*, the Court summarily dismissed an argument in *Kidwell v. U.S.*

Marketing, 102 U.S. 451, 631 P.2d 622 (1981), that the State should recover no attorney fees under Idaho Code § 52-415 (allowing "reasonable attorney's fees" arising from an action to abate a moral nuisance) because the State incurred no fees, having used salaried staff lawyers. *Id.* at 459, 631 P.2d at 630. The *U.S. Marketing* Court also cited *Furtell v. Martin*, 100 Idaho 473, 600 P.2d 777 (1979), where it found "no merit" in an argument by a losing plaintiff that the defendants could not be awarded attorney fees because they were represented by insurance counsel and hence personally incurred no fees. *Id.* at 479, 600 P.2d at 783. And in *Brown v. Matthews Mortuary, Inc.*, 118 Idaho 830, 801 P.2d 37 (1990), the appellants claimed that the respondents could not be awarded attorney fees under § 12-121 because the insurance company paid the fees. Under *Furtell*, the Court held that argument was "clearly without merit." *Id.* at 841, 801 P.2d at 48. These cases further demonstrate the error in the district court's ruling: A rule limiting the recovery of attorney fees to the amount the party actually incurred makes no sense in light of this Court's cases that allow reasonable attorney fees to parties who incur no fees at all.

4. There is yet another defect in the district court's ruling. The district court based its ruling on its perceived need to avoid conferring a "windfall profit" on the Department and imposing a penalty on the losing side. Replacement R. pp. 124-25. To the extent the court's sense of the equities drove it to limit the fees to prevent the harms it identified, this was error. In *Eighteen Mile Ranch, LLC v. Nord Excavating & Paving, Inc.*, 141 Idaho 716, 117 P.3 130 (2005), this Court rejected the district court's determination about who was and who was not a prevailing party. Having done so, the Court observed, too, that the district court's comments

about the parties' conduct during the case may have implied that the fee award reflected the court's views about "its sense of justice" in the case. *Id.* 720, 117 P.3d at 134. The Court explained that it is improper for a district court to use a fee award to "vindicate [its] sense of justice beyond the judgment rendered on the underlying dispute between the parties." *Id. quoting Evans v. Sawtooth Partners*, 111 Idaho 381, 387, 723 P.2d 925, 931 (Ct. App. 1986) (internal quotation marks omitted).

The Court has since clarified that a district court's comment about fairness would not justify reversal of a fee award determination where there was an independent and reasoned basis for its prevailing party determination. *Jorgensen v. Coppedge*, 148 Idaho 536, 541, 224 P.3d 1125, 1130 (2010). But there is, in this case, no independent, legitimate basis for the district court's ruling that prevailing parties may recover no more than they spent. The district court found that the time spent and the requested hourly rate were reasonable. But it ignored those findings and based its decision on its sense of what was fair to the other side given its perception of the costs of government lawyers to the State. The Court of Appeals has observed that "[a]n attorney fee award is not the proper place to give indirect relief from an adverse judgment," and that "[t]he arguably harsh effect of a judgment is not an appropriate "other" factor to consider in fixing attorney fees under Rule 54(e)(3)." *DeWils Interiors, Inc. v. Dines*, 106 Idaho 288, 291, 678 P.2d 80, 83 (Ct. App. 1984). In light of the court's findings, its attempt to give indirect relief to the providers by limiting the fee award to the Department is an abuse of discretion.

5. This Court's and the Court of Appeals' cases demonstrate that the district court's ruling in this case does not square with the meaning of "reasonable" under § 12-120 or

with the factors identified in Rule 54(e)(3). The Court has never limited reasonable to necessarily mean the amount actually expended. There is yet another problem with the court's ruling. By basing its decision about reasonableness on one unenumerated factor—the amount the client expends for the lawyer's services and the equities of allowing more than was spent—the district court improperly elevated it above the other, enumerated factors. *See Nalen*, 114 Idaho at 976, 763 P.2d at 1084 (even though court stated it had considered all the factors, "by allowing its decision to be controlled by only one factor," the court "deviated from proper application of" Rule 54(e)); *see also Med. Recovery Servs, LLC v. Jones*, 145 Idaho 106, 109, 175 P.3d 795, 798 (Ct. App. 2007) (court must consider each factor "without placing undue weight or emphasis on any one element").

The court's decision also improperly rendered Rule 54(e)(3)(D) (prevailing charges for like work) and (C) (skill necessary to perform the work and experience and ability of attorney) effectively irrelevant because the court found $125 an hour was reasonable under those factors, and then declined to give those findings any effect in favor of a cap that has no support in the text of the statue or rule. *See, e.g.*, *DeWils Interiors*, 106 Idaho at 290, 678 P.2d at 82 (court may not focus on "other" factors in Rule 54(e)(3)(L) to the exclusion of the "time and labor" and other factors listed in the rule); *AMX Enters., LLP v. Master Realty Corp.*, 283 S.W.3d 506, 519 (Tx. Ct. App. 2009) (awarding fees at market value consistent with factors Texas courts consider, including prevailing charges for like work). The nature of the fee agreement, specifically whether it is a fixed or contingent fee, is a factor for the court to consider. Idaho R. Civ. P. 54(e)(3)(E). But it is one factor, and it does not by itself answer the reasonableness inquiry. If

the Legislature or this Court intended fee awards to be limited as the district court limited the award in this case, either branch could through statute or rule. Neither has. A holding in this case that fees should be awarded at the prevailing rate is consistent with § 12-120 and Rule 54(e)(3). The district court abused its discretion ruling otherwise, and its award of attorney fees should be reversed.

B. This Court Should Reject the Cost-Based Approach the District Court Adopted Because It Is Riddled With Defects

1. The district court cited a Utah case, *Softsolutions, Inc. v. Brigham Young Univ.*, 1 P.3d 1095 (2000), for its cost-based approach for determining a reasonable hourly rate. Replacement R. p. 123. There, BYU litigated a case with its in-house counsel, and the court limited BYU's recovery of attorney fees to a "cost-plus" rate, rather than the prevailing market rate. The court directed the trial court on remand to undertake a complex inquiry measuring the proportionate share of the party's attorney salaries, including benefits, which are allocable to the case based on the time spent, allocated shares of overhead, which could include the costs of office space, support staff, office equipment and supplies, the law library, continuing legal education, and other "similar expenses." *Id.* at 1107. The court acknowledged that courts go two ways on this issue: Those that award fees at the prevailing market rate, and those that force parties and courts to conduct the inquiry necessary under the cost-plus standard. But, the court wrote, without much explanation,

> We are convinced that a cost-plus rate is the more reasonable measure of attorney fees to in-house counsel, and is consistent with the public policy that the basic purpose of attorney fees is to indemnify the prevailing party and not to punish the losing party by allowing the winner a windfall profit.

Id.

2. The providers will likely argue that this Court should reinterpret § 12-120 to cap reasonable fees at amounts that are actually spent and offer *Softsolutions* as the authority to follow. We have already explained that this cap is inconsistent with § 12-120, Rule 54(e)(3), and this Court's cases. That aside, there are other very good reasons why this Court should reject *Softsolutions* and the district court's ruling. For starters, the cost-based rule has very real practical problems. When the prevailing party uses pro bono or in-house counsel, or is a government entity or non-profit organization using salaried staff attorneys, the cost-plus standard requires a complicated inquiry and analysis of numerous inputs if it is to even closely approximate actual costs. The Attorney General's office would need to figure out how much of the rent, light and power bills, CLE costs, malpractice insurance, salary, Westlaw subscription, copier lease, health insurance benefits, paid time off, retirement benefits, office supplies, the Internet connection, and myriad other things are allocable to the particular attorney divided by the number of hours spent on the particular case.

Courts have characterized this enterprise as requiring an inquiry of "massive proportions"; and observed, correctly, that "[t]he problems with administering a 'cost-plus' calculus are multifarious." *Copeland v. Marshall*, 641 F.2d 880, 896 (D.C. Cir. 1980); *see also Carter v. Rhode Island Dep't of Corr.*, 25 F. Supp. 2d 24 (D. R.I. 1998) (noting complex process associated with cost-plus-based system). The administrative burden and relatively minor benefit of the cost-based approach has led many courts to decline to adopt it. *See PLCM Group v. Drexler*, 997 P.2d 511, 520 (Cal. 2000) (rejecting the view advanced in *Softsolutions*, and

explaining that the cost-plus approach is "cumbersome, intrusive, and costly to apply"); *Corbin v. Tocco*, 845 P.2d 513, 518 (Ariz. Ct. App. 1992) ("We believe it places an undue burden on the Attorney General to require the complex financial calculations to determine a figure for overhead and pro rate that figure on a per-attorney basis"); *Coleman v. McLaren*, 635 F. Supp. 266, 267-68 (N.D. Ill. 1986) ("Surely the salaries paid to the lawyers, their secretaries and other supporting staff are not the whole story. Determination and calculation of the properly allocable items of overhead and fixed costs, not only for the law offices as such but for a fairly allocable portion of the general costs of government, would be an enormously complex matter").

It is easy to imagine the administrative (read: costly) burdens to the prevailing party. But the cost-based approach could lead to a second major litigation if a non-prevailing party disputes the cost amounts and seeks discovery. Courts policing reasonableness will have to entertain arguments about the granular details of the inputs to a prevailing party's requested amount. And all for only the perception that the fee award will match the actual financial outlay a party has incurred. But actual cost has never been the keystone of the reasonableness inquiry. The California Supreme Court in *PLCM* summed up its view of the cost-based approach thusly:

> Requiring trial courts in all instances to determine reasonable attorney fees based on actual costs and overhead rather than an objective standard of reasonableness, i.e., the prevailing market value of comparable legal services, is neither appropriate nor practical; it "would be an unwarranted burden and bad public policy."

997 P.2d at 520. The California Supreme Court—and the courts rejecting the argument that the fee award must be the product of the unwieldy and expensive calculus the cost-based standard requires—have it correctly. The United States Supreme Court observed that fee petitions

"should not result in a second major litigation." *Hensley v. Eckerhart*, 461 U.S. 424, 437 (1983). That is right. But that is precisely what the district court's ruling in this case invites.

By contrast—stark contrast—adhering to an approach that considers the prevailing charges for like work rather than a limited approach that adheres to the fee agreement contains the virtue of being predictable and easy to administer. *See AMX Enters, supra*, 283 S.W.3d at 519; *Balkind v. Telluride Mountain Title Co.*, 8 P.3d 581, 588 (Colo. Ct. App. 2000) (rejecting *Softsolutions*); *Carter, supra*, 25 F. Supp. at 26; *Illinois v. Sangamo Constr. Co.*, 657 F.2d. 855, 862 (7th Cir. 1981) ("use of an objective standard of reasonableness, i.e., generally prevailing market rates, is far preferable to extensive judicial scrutiny of private fee arrangements or of the internal economics of the Attorney General's office"). The objective standard of reasonableness is not only consistent with §12-120 and Rule 54(e)(3), but it works.

So the cost-based approach is inefficient and unnecessary. But even assuming it is necessary for the award to match the cost (which under this Court's cases it is not), it is also no guarantee that the award will even match the cost. The cost-based approach fails to capture other inputs that figure into the value of legal services. Specific to this case, the SWCAP figure specifically does not capture all costs. It only captures those costs allowed by the Office of Management and Budget. Replacement R. p. 83. Plus, the SWCAP amount is flat across the office—the amount billed is the same for all deputy attorneys general; the one who makes the least and the one who makes the most are charged the same.

But even more broadly, the cost-based approach fails to account for other valuable inputs like opportunity cost. When a deputy attorney general is committed to a case, she is not

available for other cases during the time she works on the case. *See Central States*, 76 F.3d at 116 (opportunity cost factors into firm's decision whether to pursue a case or whether the cost of outside counsel is worthwhile). The cost-based approach has no answer for this cost. The cost-based approach similarly cannot be squared with cases where a client does not incur any fees, as in pro-bono or contingency fee cases. If no fees are actually incurred by the party, but the award is to the party, what then? And what about non-traditional fee arrangements where "cost" is difficult to measure in dollars? The cost-based rule prescribes different measures of allowable recovery depending on the client, her lawyer, and their fee arrangement. These differing measures are not supported by the statute, and indeed, a reasonableness inquiry that is not limited by the fee agreement avoids these problems.

3. The district court's justification for its cost-based approach—the windfall/penalty problem it perceived—is a solution in search of a problem. In short, it places the focus on the wrong target. The problem is that it assumes that reasonable attorney fees must reflect cost, instead of value. The fee a private paying party pays to its outside, private counsel necessarily includes some amount of profit, opportunity cost, and perhaps other inputs that a cost-based approach fails to account for when the lawyer is a salaried government or non-profit or in-house lawyer. The sum of those inputs represents the value of the services. But by awarding fees to match cost instead of value, the district court distinguishes the recoverable fee based on who the lawyer and who the client are, and for no good reason. Under Rule 53(e), the focus is on the value of legal services; that is, reasonableness is concerned with what is objectively reasonable in the particular case, with consideration of, among other factors, the

prevailing charges for like work. The prevailing charges for like work in the relevant geographic market represents the value of those legal services regardless of whether the lawyer performing those services is at a large firm, small firm, government entity, non-profit legal organization, corporate law department, or works on contingency. By design, the statute and rule do not seek a determination that necessarily represents the actual cost of the legal services. The perceived evil the district court sought to avoid—a "windfall" to the government—thus does not exist. There is no windfall and no penalty just because a losing party pays more in fees than the winning party spent. Indeed, as we have explained, a reasonable fee, under this Court's cases, contemplates precisely that a losing party may pay more in attorney fees than the winner paid.

As the U.S. Supreme Court has said, "[a] 'reasonable attorney's fee' [is] reasonable compensation, in light of all the circumstances, for the time and effort expended by the attorney . . . , no more and no less." *Blanchard v. Bergeron*, 489 U.S. 87, 93 (1989). Why should a losing party be entitled to a discount from reasonable, market-based fees simply because the winner is the government or a party that used in-house or salaried counsel? *See Blum v. Stenson*, 465 U.S. 886, 895 (1984) (fee award under 42 U.S.C. § 1988 to plaintiff represented by legal aid organization should be based on prevailing market rates; rejecting argument that prevailing market rates created a "windfall"); *PLCM, supra,* 997 P.2d at 520 (rejecting "windfall" argument); *Corbin, supra*, 845 P.2d at 518 (rejecting argument that market rate award will unjustly enrich state); *Harris v. Marsh*, 123 F.R.D. 204, 227 (E.D. N.C. 1988), *aff'd in part, rev'd in part on other grounds sub nom. Blue v. U.S. Dep't of the Army*, 914 F.2d 525 (4th Cir. 1990) (no reason "[w]hy government counsel, who work on the same basis, should be treated

any differently than [salaried] counsel"); *Coleman, supra*, 635 F. Supp. at 267-68 (market-rate basis for attorney fee award "is a two-way street" and it "makes no difference" that the "defendants' attorneys are public servants who will not personally receive any fees"); *Central States*, 76 F.3d at 116 (finding no justification to limit fee recovery to pension fund's out-of-pocket costs). Losing a case against the State with state-salaried lawyers is already cheaper than it is to lose to a party who hires outside, private counsel. *See Dep't of Transp. v. Grathol, supra*, 158 Idaho at 55, 343 P.3d at 497 (J. Jones, J., specially concurring) (noting costs of defense of condemnation action would be "substantially less" had the State been able to use its own lawyers). Had the providers won this case they surely would have demanded market-based fees. There is no good reason to deny the State the same basis on which to seek fees.

II. The Department is Entitled to Attorney Fees for This Appeal Under Idaho Code § 12-120(3)

As the district court correctly determined, this case concerned a commercial transaction. The providers contracted with the State to provide Medicaid services, and all the providers' claims arose from that transaction. The district court's determination that the claims arose from a commercial transaction has not been appealed. Thus, § 12-120(3) applies, and, if the Department prevails on appeal, it should be entitled to an award of attorney fees for the appeal. *See Garner v. Povey*, 151 Idaho 462, 471, 259 P.3d 608, 617 (2011) (where action was based on commercial transaction, prevailing party was entitled to attorney fees on appeal under § 12-120(3)).

CONCLUSION

This Court should reverse the district court's award of attorney fees and remand with

instructions to award the Department attorney fees in the amount requested, $74,925.00. This Court should also award the Department reasonable attorney fees under Idaho Code § 12-120(3).

Dated February 16, 2016.

STATE OF IDAHO
OFFICE OF THE ATTORNEY GENERAL

By: _____
CARL J. WITHROE
Deputy Attorney General
Attorneys for Cross-Appellants

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on this 16th day of January, 2016, I caused to be served a true and correct copy of the foregoing by the following method to:

Dennis M. Charney
CHARNEY AND ASSOCIATES, PLLC
1191 East Iron Eagle Drive
Eagle, Idaho 83616

☒ U.S. Mail
☐ Hand Delivery
☐ Certified Mail, Return Receipt Requested
☐ Overnight Mail
☐ Facsimile

_____
CARL J. WITHROE
Deputy Attorney General